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THE ARETÉ QUARTERLY

Inside This Issue

Welcome

The investment landscape continues to evolve and as it does, fresh approaches are needed in order for investors to be able to derive the greatest benefit at the lowest cost. At Areté we are constantly challenging conventions, leveraging technology and creatively seeking new solutions such that investors have the greatest chance possible to get ahead. Please take a look at our blog [here] where we regularly post our thoughts and also please always feel free to contact us with questions or comments.

Business Update

Every once in a while, it's good to take a step back, take a deep breath, and get some perspective on things. Or simply to ask, "What was the question again?"

For Areté the question has always been, "How can we best apply our expertise to help investors get ahead? This perspective is grounded in the classic marketing insight by Harvard's Theodore Levitt that "people don't want to buy a quarter-inch drill. They want a quarter-inch hole." In other words, people hire a product or a service to do a certain "job".

My contention has been, and continues to be, that people don't want to buy a massive array of investment products and services. Rather, the "job" they want done is to be reasonably secure that they will be able to look forward to a decent retirement after many years of work.

Unfortunately that "job" has gotten a lot harder. A number of challenges were addressed in a recent piece in the *Financial Times* by Lisa Pollack [here]. She noted, "There is, however, a growing group of people like me [i.e., younger] … for whom retirement is a vague ambition likely to be further undermined by future deficits, changes to the retirement age, additional unfavourable alterations to the state pension and low interest rates. We are in a different emotional and mental situation from fiftysomethings on DB schemes. And we need more information that's relevant to us."

These comments are telling in many ways, and not just for younger investors. For one, they reveal with unusual honesty the severity of today's investment challenges. Multiple forces are "undermining" retirement plans, each of which is powerful in its own right.

Secondly, the fact that the concept of retirement has evolved from a near certain goal to a "vague ambition" highlights the

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degree to which the future is less bright for younger investors than older ones (i.e., declining intergenerational equity). When one group of people is treated unfairly relative to another group of people, the cohesiveness of society erodes and political (and therefore, economic) uncertainty increases. We don't need to look past this year's election to see this phenomenon.

Finally, the comment that, "we need more information that's relevant to us" sounds a lot like unmet demand - and therefore an interesting business opportunity for Areté. I actually think that a lot of investors have been underserved for quite a while, but the immediate pain has been forestalled by the anesthetic of easy monetary policy. By incorporating a different trajectory for their futures, younger investors see something many others don't: There is a need for a fundamentally different approach to investment services.

This is good news for Areté because it plays right into our strengths – staying focused on the "job" that investors want done.

This was exactly the reason for starting up the personal Chief Investment Officer service. The service is designed to provide "more information that's relevant" to investors whether they be individuals or organizations. It is also designed to do so in a way that is very modular and accessible in order to make it as easy as possible for investors to get that relevant information.

In addition, during this period in which opportunities for stocks have been meager (see "Transaction Reivew"), I have been allocating more of my time to building up the set of analytical tools from which to draw upon when market opportunities do emerge again.

Most specifically, I have been building a proprietary valuation model to replace the one I used to license from a vendor. New technology and better access to data play right into Areté's strengths and are facilitating not just much greater control over the valuation exercise, but also the potential for some pretty exciting future development and at a lower operating cost.

While I believe that Areté's technology and research roadmaps are fairly unique, they are also emblematic of the ongoing effort to gather, manage, and communicate "relevant information" for investors.

Finally, there is a wave of change coming. I thought it would come sooner, but make no mistake, it is coming. As investors demand better ways to get "more information that's relevant" to them, and in an easy and cost-effective way, there will be serious challenges for many providers. But there will also be terrific opportunities for some new ones.

Thanks for your interest and take care!

David Robertson, CFA
CEO, Portfolio Manager

Portfolio Characteristics – Areté Mid Cap Core

A key proposition for Areté's Mid Cap Core strategy is that it is a truly representative mid cap portfolio. In general, this suggests that over time, you can expect to see the aggregate characteristics and sector exposures of the strategy migrate to those of the Russell Midcap Index®. During intervening periods, however, sector exposures and other characteristics will reflect the opportunities we find in the market at that point in time.

We believe maintaining a truly representative mid cap portfolio is important for two reasons. First, a truly mid cap portfolio faithfully plays its role in a broader asset allocation scheme. Second, it allows for accurate assessment of performance. Without an appropriate benchmark it is difficult, if not impossible, to judge whether performance differentials are due to skill or luck, and are sustainable or transient.

For example, many fund managers attempt to beat their benchmark by timing the market and/or migrating style. These tactics rarely generate sustainble out-performance. To us, such activities usually just serve to obfuscate the underlying inability of the manager to add value through a coherent and disciplined investment process.

All of that said, our overarching goal is to provide attractive returns to investors on an *absolute* basis. During most times, the stock market provides an attractive vehicle through which to realize those returns. In unique periods of significant overvaluation, however, when our valuation and other analyses suggest attractive returns are less likely, we may allow the cash portion of the portfolio to increase so as to preserve investors' capital and retain the option to buy cheaper in the future.

Portfolio characteristics for the quarter continue to confirm that the equity portion of AMCC is a very representative mid cap portfolio. Market caps for AMCC are fairly similar to the mid cap index although the median is now considerably smaller. AMCC is considerably cheaper on the bases of Price-book and Price-sales which tend to be more stable metrics.

Portfolio Characteristics (09/30/16)

	Arete MCC*	Midcap Index**
Size		
Average Market Cap ($ mil.)	8,137	8,468
Median Market Cap ($ mil.)	4,704	6,393
Minimum Market Cap ($ mil.)	525	214
Maximum Market Cap ($ mil.)***	33,524	50,163
Number of holdings	20	796
Valuation		
P/E current year	22.1	24.2
P/B	2.8	4.5
P/S	1.0	2.1
Yield (%)	3.8	3.1
Valuation drivers		
ROE (%)****	8.2	10.8

Source: Calcbench
**Note:* Excludes positions which are less than 0.1% weights.
***Note*: Arete currently does not subscribe to the Russell Indexes and therefore the statistics presented here represent approximations of the Russell Midcap® Index.
****Note*: Stocks with low floats are excluded
****Note: The measure of ROE was changed from the average to the median as of 3/31/14.

As a note, we recently started using financial data provided by Calcbench. Historically we used data from our valuation vendor, Applied Finance Group. As a result, there may some modest differences that cause imperfect comparisons.

Sector exposures are all below benchmark weights due to the high cash position. Cash has remained at fairly high but stable levels over the last several quarters.

As a quick reminder, active share highlights the degree to which a portfolio's holdings differ from its benchmark. A portfolio must differ significantly from its benchmark in order to significantly outperform it — and therefore to justify charging active management fees. Areté's Mid Cap Core portfolio consistently exhibits active share well above the 80% level considered to be very active.

Sector exposure (percent of assets on 9/30/16)

Economic sector***	Arete MCC*	Midcap Index**	Percentage Comparison
Consumer Discretionary	1.1	15.9	6.9%
Consumer Staples	0.0	5.3	0.0%
Energy	0.0	6.2	0.0%
Financials	10.5	11.8	89.2%
Health Care	5.0	10.0	50.0%
Industrials	2.9	12.4	23.4%
Information Technology	1.6	15.0	10.7%
Materials	4.5	5.6	80.0%
Real Estate	5.6	10.4	53.6%
Telecommunications	0.0	1.0	0.0%
Utilities	2.5	6.4	39.3%
Equity exposure	33.7	100.0	
Cash and equivalent	66.3	0.0	

Source: Calcbench
**Note*: Arete Mid Cap Core is represented by the aggregate of all assets in the composite at the given date.
***Note*: Arete currently does not subscribe to the Russell Indexes and therefore the sector weights presented here represent approximations of the Russell Midcap® Index.
****Note*: Economic sector classifications were changed from Russell to GICS beginning Q414.

Active share* (9/30/16)

Period	Percent**
Q216	96.3
Q216	96.1
Q116	96.2
Q415	96.6
Q315	92.3

**Note*: Computed for AMCC composite
***Note*: Active share > 80% is considered "very active"

Transactions review – Areté Mid Cap Core

Although there were no transactions in the quarter, as we have mentioned several times in the past, we remain diligent in looking for new opportunities but continued to be foiled by excessively high valuations.

The breadth of these challenges was illustrated nicely by John Hussman [here]: "Put simply, the reason that the capitalization-weighted S&P 500 was more richly valued in 2000 is that its largest, highest price/revenue components were breathtakingly overvalued. Yet if investors didn't want to invest in hypervalued tech stocks, they still had somewhere else to go. That's not true today."

He concluded, "What's notable here is that unlike 2000 and even 2007, when at least some of the valuation deciles were trading at somewhat reasonable valuations, we currently observe a situation where investors effectively have nowhere to go. Even the decile with the best *relative* valuation is at the most extreme level in history."

This analysis articulates our views well. Whereas some undervalued opportunities existed in 2000 and 2008, exceptionally few are available today. As a result, we continue to hold a lot of cash and wait for better opportunities.

Performance review – Areté Mid Cap Core

The Areté Mid Cap Core product is designed with the flexibility to invest in the most attractive mid cap stocks, regardless of any particular "style" designation. With that context, the primary criterion for selecting a stock in the Mid Cap Core strategy is that market value is significantly less than our estimate of intrinsic value. In other words, we try to find situations in which our research generates expectations for a company's growth and profitability that justify substantially greater valuations than what the market discounts.

Our investment process is designed to discover, analyze, and assemble stocks into a diversified portfolio that consistently outperforms its benchmark over time. Specifically, our investment objective is to outperform the benchmark Russell Midcap® Index by 200-400 basis points per year, net of fees, over the course of a market cycle.

Our target of 200-400 basis points of outperformance is based upon our experience with the strategy and upon our judgment of value creation. Our goal is to outperform by a large enough margin relative to risk to clearly merit the cost in time and resources to evaluate investing with us.

Areté's Mid Cap Core (AMCC) strategy returned .83% (net of fees) for the quarter versus 4.52% for the Russell Midcap Index® (RMC) (see pages 8 – 10 for performance and related disclosures). AMCC continues to underperform when the market races higher due to its high cash position, but that cash also provides a significant buffer against material downside.

Once again, broad market trends and directional bets tended to have a far greater impact on stocks than individual company performance. As the market priced in a an increasing likelihood of a rate hike by year end, NRG, AUY, and DVA were hurt but AMTD was helped. RGLD was notable for bucking the negative trend among gold stocks.

NRG and SHLD also suffered from credit concerns. While the concerns regarding the GenOn subsidiary for NRG and the poor July quarter for SHLD were warranted, the reaction also demonstrated the acute sensitivity of the market to bad news, especially among stocks that are not large ETF components.

Stock performance* (6/30/16 - 9/30/16)

Best performers

Company	Return in quarter (%)
Genworth Financial	92.3
Seagate Technology	58.3
TD Ameritrade	23.8
Oshkosh Corp	17.4
Royal Gold	7.5

Worst performers

Company	Return in quarter (%)
NRG Energy	-25.2
Yamana Gold	-17.1
Sears Holdings	-15.8
Davita Inc	-14.6
Mylan Inc	-11.8

**Note*: Performance includes price changes only; it does not include dividend income in the quarter.

The most notable company specific performance occurred with GNW which spiked up as merger activity increased in the mortgage insurance sector. While there was nothing new about this activity or with GNW's exposure to mortgage insurance, the strong reaction highlighted the value of GNW's franchise. To an important extent, however, the move also reflected the directional nature of many participants in this market as GNW had been oversold earlier on concerns about its long term care business. In a similar vein, STX had a nice quarter but was just bouncing off of weak results last quarter after which the stock got pounded.

MYL had the most notable company specific performance among underperformers as it made headlines for dramatic price increases in its icononic Epi-pen product as well as for overcharging Medicaid. Concerns over potential penalities dogged the stock in the second half of the quarter, but were resolved in a settlement after the end of the quarter.

Investment Philosophy

We firmly believe in the critical importance of a cogent investment philosophy for any investment operation. In order to emphasize this point, and to assist you in understanding how we work, we provide an abbreviated version of our investment philosophy here. The text of our investment philosophy is also provided, in its entirety, in our Form ADV, Part II which is available upon request at any time.

Performance derives from exploiting mispriced securities.

The key to investment performance is finding and exploiting market inefficiencies in the form of mispriced securities. There are two components to this. One component involves determining the fair price of securities in the form of underlying intrinsic value, which we do primarily through calculating discounted cash flows.

The second component of exploiting mispriced securities is establishing a clear understanding as to the various mechanisms at work that allow mispricing to occur. By understanding the mechanisms and motivations of the marginal buyer and seller, we believe we can more accurately estimate the probabilities and expected values of investment opportunities.

Nobody has perfect information.

Competitive pressure and technological development have conspired over the years to make most data and analysis commodities which no longer provide a meaningful competitive advantage. What can provide an advantage, however, is *how* that information is used and *how* it gets interpreted in making investment decisions.

In order to convert the raw material of information into the useful output of a good investment decision, it is necessary to assimilate and synthesize the information into some meaningful form. We believe the most effective way to accomplish this is to thoughtfully deploy resources available according to the nature of the research tasks at hand.

Research culture and research prioritization are also important in relation to analyzing and synthesizing information. We believe that the best way to leverage the collective knowledge and experience of a research team is to encourage active and open dialogue designed to explore multiple perspectives and to challenge individual assumptions, biases, and beliefs. Only by enduring such scrutiny do the best ideas rise to the top. Further, in order to fully leverage these ideas, we believe research efforts must be dynamic and flexible in allocating resources such that ideas receive attention in proportion to the expected benefit to the portfolio.

Execution is crucial for investment success.

In order to create value, an investment strategy needs to be implemented continuously and comprehensively. Actions speak louder than words. We believe the most effective efforts focus on a few simple, but key concepts that work to ensure proper execution of a firm's investment strategy.

The first key to execution is structural in nature and involves a firm's independence. By maintaining independent ownership, an investment firm eliminates agency effects which can present a conflict of interest between clients and certain of its ownership groups. Independent ownership ensures that client and manager interests are optimally aligned.

The second key to execution is temperament. The best investors tend to have a temperament that provides them the courage and initiative to act, often going against the grain, when opportunities arise. However, the same temperament provides balance such that decision-making is not simply a risk-taking activity, but a very conscious and targeted effort to engage in propositions with high risk-adjusted expected returns.

Finally, another important element of execution is simply doing what you say you do in your investment process. Too often, perfectly acceptable investment processes fail when actual investment activities bear little resemblance to the process described in the marketing presentation. We call this the "marketing gap;" the difference between what is said and what is done. Execution is optimized when the marketing gap is minimized.

Areté Mid Cap Core Composite

Arete Asset Management, LLC
Mid Cap Core Composite
July 31, 2008 - September 30, 2016

Period	Gross-of-Fees Return (percent)	Net-of-Fees Return (percent)	Russell Midcap® Index Return (percent)	Number of Portfolios	Internal Dispersion (percent)	Total Composite Assets ($)	Composite Assets With Bundled Fees ($)	Percentage of Composite Assets With Bundled Fees	Total Firm Assets ($)
2008*	-37.97	-38.16	-35.01	$3	NA	207,031	207,031	100%	207,031
2009	48.63	47.83	40.48	3	NA	471,867	471,867	100%	673,806
2010	16.86	15.78	25.48	3	NA	546,315	546,315	100%	877,368
2011	-8.20	-8.88	-1.55	3	NA	497,767	797,767	100%	897,918
2012	15.20	13.84	17.28	4	NA	798,766	798,766	100%	897,341
2013	23.18	22.00	34.76	4	NA	974,605	974,605	100%	1,172,496
2014	4.01	2.99	13.22	4	NA	1,003,729	1,003,729	100%	1,200,564
2015	-7.56	-8.44	-2.44	4	NA	919,035	919,035	100%	1,206,652
2016									
January	-3.21	-3.46	-6.55	4	NA	887,219	887,219	100%	1,172,245
February	1.48	1.48	1.13	4	NA	900,330	900,330	100%	1,188,694
March	3.60	3.60	8.19	4	NA	932,773	932,773	100%	1,223,729
April	1.43	1.18	1.06	4	NA	943,800	943,800	100%	1,238,672
May	-0.57	-0.57	1.64	4	NA	938,449	938,449	100%	1,230,777
June	0.59	0.59	0.46	4	NA	944,009	944,009	100%	1,238,757
July	2.16	1.92	4.57	4	NA	962,120	962,120	100%	1,259,212
August	-1.87	-1.87	-0.25	4	NA	944,144	944,144	100%	1,238,454
September	0.82	0.82	0.20	4	NA	951,865	951,865	100%	1,247,116
Q1	1.76	1.49	2.24	4	NA	932,773	932,773	100%	1,223,729
Q2	1.46	1.20	3.18	4	NA	944,009	944,009	100%	1,238,757
Q3	1.08	0.83	4.52	4	NA	951,865	962,120	100%	1,247,116
YTD	4.36	3.56	10.26	4	NA	951,865	944,009	100%	1,247,116

**Note*: Peformance through 12/31/08 is from inception of composite on 7/31/08.

Areté Asset Management Mid Cap Core performance composite disclosures follow:

Compliance statement

Areté Asset Management has prepared and presented this report in compliance with the Global Investment Performance Standards (GIPS®).

Definition of the firm

Areté Asset Management, LLC (Areté) was established in 2008 and is registered as an investment adviser in the state of Maryland. Areté is defined as an independent investment management firm and is not affiliated with any parent organization. Areté currently manages one strategy, the U.S. equity mid cap core strategy, which it markets to individual and institutional clients.

Areté Asset Management Mid Cap Core performance composite disclosures continued:

Benchmark
The benchmark is the Russell Midcap® Index and its performance is reported in U.S. dollars.

Calculation methodology

Portfolio valuations are calculated as of calendar month-end and are computed in U.S. dollars and performance is also reported in U.S. dollars. Time-weighted rates of return are used which adjust for external cash flows. Our smaller, retail accounts contain fee structures in which one flat, per-transaction fee is charged for trading expenses and which embeds an implicit charge for custody. Since trading and custody charges cannot be directly segregated in these cases, they constitute “bundled fees”. Gross-of-fees performance returns are presented before management and custodial fees when custodial fees can be segregated from trading, but are presented before management fees and after bundled (trading and custodial) expenses for our retail accounts. Net-of-fees returns are presented after management fees, trading expenses, and custodial expenses are deducted or after management fees and bundled (trading and custodial) fees for retail accounts. There are no instances in which management fees are bundled with trading or custodial fees. Returns are presented net of nonreclaimable withholding taxes when applicable. Areté does not use leverage or derivatives in the management of portfolios. Additional information regarding policies for calculating and reporting returns is available upon request.

The composite
This U.S. Equity Mid Cap Core composite was created in August, 2008 and includes all fee-paying, taxable and non-taxable, discretionary, long only, fully invested portfolios benchmarked to the Russell Midcap Index. Every new portfolio is added to the composite in the first complete calendar month that it is “fully invested”. For purposes of composite construction, a portfolio is “fully invested” if its equity composition is greater than 90% of the equity composition of the composite. Each portfolio will remain in the composite until its equity composition becomes less than 90% of that of the composite. A complete list and description of firm composites is available upon request.

*As of March 31, 2012, the composite has been redefined in order to clarify policy in light of unusually high cash positions recently. Prior to March 31, 2012, a portfolio was considered to be “fully invested” if greater than 90% of portfolio assets were invested in equity securities which implicitly assumed a nearly 100% equity position in the composite.

Fee schedule
The management fee schedule is as follows: 1% of AUM up to $1 million, 0.75% on AUM greater than $1 million, but less than $5 million, and 0.65% on assets greater than $5 million.

Areté Asset Management Mid Cap Core performance composite disclosures continued:

Minimum account size
There is no minimum account size for inclusion in the composite. Please note, however, the minimum initial account size accepted is $100,000.

Dispersion
Internal dispersion is currently not meaningful as there are five or fewer portfolios included in the composite. In the future, we plan to calculate dispersion using the dollar-weighted standard deviation of all portfolios included in the composite for each performance period.

Verification
Areté has not been verified by an independent verifier for its compliance with GIPS.